

COMMENT LETTER

March 27, 2017

ICI Submits Comment Letter on Proposed Amendments to FINRA Rule 2210 (pdf)

March 27, 2017 Marcia E. Asquith Office of the Corporate Secretary FINRA 1735 K Street, NW Washington, D.C. 20006-1506 Re: Communications with the Public, FINRA Regulatory Notice 17-06 (February 2017) Dear Ms. Asquith: The Investment Company Institute¹ appreciates the opportunity to comment on FINRA's proposed amendments to FINRA Rule 2210 (Communications with the Public) (the "rule").² FINRA's proposal follows from its 2014 retrospective review of the rule and other communications with the public rules, which was intended to assess their effectiveness and efficiency.³ 1 The Investment Company Institute (ICI) is a leading global association of regulated funds, including mutual funds, exchange-traded funds (ETFs), closed-end funds, and unit investment trusts (UITs) in the United States, and similar funds offered to investors in jurisdictions worldwide. ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. ICI's members manage total assets of US\$18.9 trillion in the United States, serving more than 95 million US shareholders, and US\$1.6 trillion in assets in other jurisdictions. ICI carries out its international work through ICI Global, with offices in London, Hong Kong, and Washington, DC. 2 FINRA Requests Comment on Proposed Amendments to Rules Governing Communications With the Public, FINRA Regulatory Notice 17-06 (February 2017) (the "proposal"), available at www.finra.org/sites/default/files/notice_doc_file_ref/Regulatory-Notice-17-06.pdf. 3 FINRA Requests Comment on the Effectiveness and Efficiency of its Communications with the Public Rules, FINRA Regulatory Notice 14-14 (April 2014), available at www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p479810.pdf. Marcia E. Asquith March 27, 2017 Page 2 We support FINRA's proposal. If adopted, it would permit FINRA member firms to provide their customers with investment planning illustrations, which could help inform customers' investment decision-making. In addition, we recommend that FINRA enhance the proposal further by: (i) removing the "customization" requirement; and (ii) providing guidance regarding the precise scope of the proposed and existing exceptions to the rule's general prohibition on projections. I. Description of the Proposal The rule generally prohibits communications that predict or project performance, subject to certain exceptions.⁴ The proposed amendments would create a new exception to this general prohibition: one for a "customized hypothetical investment planning illustration that projects performance of an asset allocation or other investment strategy and not an individual security." Use of this exception would be conditioned upon (i) there being a "reasonable basis for all assumptions, conclusions and

recommendations;” and (ii) providing clear and prominent disclosure that the illustration is hypothetical; that there is no assurance that the performance or event will occur; and that includes all material assumptions and limitations. The proposed amendments also would include related supervisory requirements. II. ICI’s Comments on the Proposal We support FINRA’s proposal. In crafting it, FINRA recognized both the rule’s investor protection aims and the informational benefits that illustrations may provide to investors. Illustrations can be very useful to investors who are seeking to achieve future financial objectives (e.g., financing retirement or college education) and need assistance in determining how to do so. FINRA could improve the proposal in two ways, however. First, the proposal would permit only a “customized” illustration, which FINRA describes as “one designed for a particular client or multiple clients who share an account.” This would limit unduly the efficacy of this exception. We see no policy reason for requiring customization, particularly given the disclosures that would accompany the illustrations and the supervisory review requirements. (Indeed, supervisory review becomes easier when illustrations are more general and broadly disseminated.) While having the ability to customize illustrations is no doubt beneficial (e.g., the illustrations could show customer-specific investment sums, goals, and time horizons), more general illustrations also may be useful to investors. For instance, general illustrations provided to multiple investors can highlight important investment concepts such as variability of investment returns, differences in rates of return among asset classes, ways in which asset classes with different performance correlations might be combined to reduce overall portfolio volatility, and the benefits of compound returns over long time horizons. Specifically, the rule permits hypothetical illustrations of mathematical principles, investment analysis tools (or the written reports they produce), and price targets in research reports. Marcia E. Asquith March 27, 2017 Page 3

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5 The rule should permit these types of general illustrations to the same extent that it permits customized illustrations, with each subject to the same safeguards. Second, FINRA should clarify the scope of the new—and existing—exceptions. Given the ambiguity of their scope, the existing exceptions (particularly the hypothetical illustrations of mathematical principles and investment analysis tools exceptions) have in practice proved to be somewhat limited in the relief that they provide. For instance, in our comment letter on FINRA’s retrospective rule review⁶ we recommended that FINRA provide additional clarity with respect to the use of output from investment analysis tools within educational materials. We pointed out that a member may use the output from an investment analysis tool (e.g., illustrations of the interplay between different asset allocations and different asset withdrawal rates in retirement, and their expected results) in educational materials, and a question existed as to whether the investment analysis tool exception would apply to those materials.⁷ This is just one example of challenges members have faced in interpreting and using the current exceptions in ways that benefit investors. It is possible that the types of general illustrations described above (which could be included in educational materials or otherwise) could fit within one of these existing exceptions. But this is not entirely clear, and members may be reticent to create and use materials of a type that FINRA has not broadly and publicly identified as permissible. FINRA should confirm that these types of practices—designed to educate investors about key investment principles—are consistent with the rule. Both investors and FINRA members would benefit from this additional clarity, which presumably would lead to increased use of tools, illustrations, and materials that improve investor education and comprehension. FINRA appears to be motivated, at least in part, by the recognition that the SEC regulates presentation of projections differently under the Investment Advisers Act of 1940 than FINRA does under the rule. We believe there is more work to do in harmonizing these sometimes-inconsistent practices. 5 Cf. Acting SEC Chairman Michael S. Piwowar, Remarks at the “SEC Speaks” Conference 2017: Remembering the Forgotten Investor (Feb. 24, 2017)(explaining the importance to

investors of concepts such as risk-return tradeoffs and modern portfolio theory), available at www.sec.gov/news/speech/piwowar-remembering-the-forgotten-investor.html. 6 Letter from Dorothy Donohue, Acting General Counsel, ICI, to Marcia Asquith, Office of the Corporate Secretary, FINRA, dated May 23, 2014, available at www.finra.org/sites/default/files/NoticeComment/p519148.pdf. 7 We understood that FINRA appeared to permit this practice, however, provided that: (i) no investment products are mentioned (whether generically or specifically); (ii) the recipients of the material have access to one of the member's online investment analysis tools; (iii) the material "advertises" the proprietary investment analysis tools that are available on the member's web site; and (iv) the material shows multiple outcomes and allows the investor to "interact" with the printed charts (e.g., the investor may select their own withdrawal rate, asset allocation, and number of years in retirement and find the resulting probability of success). We encouraged FINRA to formalize this position in the rules. Marcia E. Asquith March 27, 2017 Page 4 standards. Still, adoption of the proposed amendments—particularly if FINRA enhances the proposal as outlined above—would be a welcome first step. ■ ■ ■ ■ ■ We appreciate having the opportunity to comment on the proposal, and we stand ready to assist FINRA in any way that we can. If you have any questions, please contact me at (202) 218-3563 or Matthew Thornton at (202) 371-5406. Sincerely, /s/ Dorothy Donohue Deputy General Counsel